

Message Text

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AMEMBASSY DOHA

AMEMBASSY JIDDA

AMEMBASSY KABUL

AMCONSUL KARACHI

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MANILA FOR USADB

E.O. 11652: N/A

TAGS: ECON, PK

SUBJECT: PAKISTAN: ECONOMIC ASSESSMENT OF 1974 AND 1975
(PART I OF II)

1. SUMMARY: AS FOR MOST OTHER COUNTRIES, 1974 WAS A BAD

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YEAR ECONOMICALLY FOR PAKISTAN. IT MADE NO PROGRESS TOWARD

LEAVING THE RANKS OF THE LDC'S. ALTHOUGH STARVATION NEVER THREATENED, PER CAPITA GNP GROWTH WAS PROBABLY ZERO. VARIOUS NATURAL CALAMITIES, A WORSENING BALANCE OF PAYMENTS, THE CONTINUED ADJUSTMENT OF THE INDUSTRIAL SECTOR TO THE ECONOMIC REFORMS OF 1972, PLUS A WARY PRIVATE SECTOR, PREVENTED ANY ECONOMIC LEAP FORWARD. THE PROSPECTS FOR 1975 ARE UNFORTUNATELY FOR LITTLE IMPROVEMENT. THERE WAS ONE ENCOURAGING NEW DEVELOPMENT: MASSIVE AND UNEXPECTED INPUTS OF AID FROM THE OIL-RICH MIDDLE EASTERN COUNTRIES. THIS NEW AID SOURCE PROMISES TO CONTINUE AND GIVES PAKISTAN HOPE FOR A BRIGHTER FUTURE. THE IMPLICATIONS FOR THE U.S. OF THE PAKISTAN ECONOMIC SITUATION ARE DISCUSSED IN PART II SEPTEL (NOTAL). END SUMMARY.

2. PRIME MINISTER BHUTTO HAS SAID THAT HE WAS RELIEVED TO SEE 1974 PASS. MUCH ECONOMIC MISFORTUNE HAD STRUCK THE COUNTRY: THE EXPORT MARKET FOR RAW COTTON AND YARN HAD COLLAPSED; INSTEAD OF NEARING SELF-SUFFICIENCY IN WHEAT, PAKISTAN WAS HAVING TO IMPORT AS MUCH AS 1.5 MILLION TONS; THEN THERE WAS THE DROUGHT AND THE TARBELA DAM DAMAGE; ALL OF THIS BEING FINALLY CAPPED BY THE SWAT EARTHQUAKE DISASTER. THE PRIVATE SECTOR, PUT OFF BY THE NATIONALIZATION ACTIONS AND GOVERNMENT CURBS OF THE LAST THREE YEARS, CONTINUED CAUTIOUS ABOUT RESUMING NEW LARGE SCALE INVESTMENT. NO SIGNIFICANT NEW PRIVATE FOREIGN INVESTMENT TOOK PLACE.

3. WHAT BHUTTO DID NOT DRAW ATTENTION TO WAS THAT THERE ALSO OCCURRED SOME HEARTENING NEW DEVELOPMENTS THAT GIVE HOPE FOR THE FUTURE. THE PRINCIPAL ONE HAS BEEN THE PHENOMENAL INCREASE IN AID FROM THE OIL-RICH MIDDLE EASTERN COUNTRIES WITH MORE PROBABLY TO COME. DURING THE YEAR, CASH OR COMMITMENTS FROM THESE SOURCES EXCEEDED \$800 MILLION, OF WHICH DISBURSEMENTS CAME TO \$290 MILLION. GOP ECONOMIC OFFICIALS ARE JUBILANT ABOUT THIS NEW SOURCE OF LARGESSE AND ARE CONFIDENT THAT IT CAN CONTINUE TO BE TAPPED AS LONG AS THESE COUNTRIES ARE ENJOYING THEIR PRESENT INFLOWS OF WEALTH. ALSO HEARTENING WAS THE FACT THAT WITH THE DEPARTURE OF LEFTIST FINANCE MINISTER MUBASHIR HASAN THE GOVERNMENT IS NOW COMPOSED OF PRAGMATIC LEADERS WHO APPEAR TO BE TRYING TO EXECUTE SENSIBLE ECONOMIC POLICIES. AS AN IBRD TEAM MEMBER REMARKED PRIVATELY LAST NOVEMBER. "YOU CANNOT HELP LIMITED OFFICIAL USE

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BUT FEEL SYMPATHETIC FOR THIS COUNTRY. ITS LEADERS ARE GENERALLY TRYING TO DO ALL THE RIGHT THINGS."

4. THUS, WHILE CY 1974 WAS NOT A GOOD YEAR AND CY 1975 WILL LIKELY SHOW NO IMPROVEMENT, THE LONGER TERM PROSPECTS FOR THIS COUNTRY SEEM REASONABLY GOOD. THE COUNTRY HAS THE POTENTIAL OF BECOMING SELF-SUFFICIENT IN FOOD, ITS LEADERSHIP IS FOLLOWING GENERALLY COMMENDABLE ECONOMIC POLICIES, THERE

IS A FAIR POSSIBILITY OF A REVERSAL OF THE DOWN TREND IN PRIVATE INVESTMENT, AND OIL EXPERTS ARE HOPEFUL THAT NEW OIL FIELDS CAN BE FOUND, TO SUPPLEMENT THE COUNTRY'S RICH GAS FIELDS. FOR AN LDC, THE PROBLEMS HERE DO NOT SEEM UNSURMOUNTABLE. THERE IS A WIDESPREAD FEELING THAT LIVING STANDARDS CAN AND WILL GRADUALLY IMPROVE.

5. THERE ARE FOUR TRADITIONAL MEASURES OF HOW A COUNTRY IS FARING ECONOMICALLY: BY ITS GROWTH RATE, ITS RATE OF UNEMPLOYMENT, ITS PACE OF INFLATION, AND ITS BALANCE OF PAYMENTS. IF WE EXAMINE PAKISTAN'S PERFORMANCE BY THESE FOUR MEASURES (SEE BELOW), WE SEE HOW DISAPPOINTING 1974 WAS AND THAT 1975 WILL ALSO BE A TOUGH YEAR.

6. GROWTH. WE ESTIMATE PAKISTAN'S REAL GROWTH RATE IN CY 1974 WAS PROBABLY AROUND THREE PERCENT, WHICH WOULD BE LOWER THAN THE PREVIOUS YEAR AND CERTAINLY BELOW THE OVERALL LDC GROWTH AVERAGE OF 6.2 PERCENT IN RECENT YEARS. PER CAPITA LIVING STANDARDS PROBABLY DID NOT RISE AT ALL BECAUSE POPULATION WAS ALSO GROWING AT A THREE PERCENT RATE. THE REASONS FOR THIS DISAPPOINTING PERFORMANCE HAVE ALREADY BEEN MENTIONED. FORTUNATELY, LABOR WAS GENERALLY QUIESCENT AND STRIKES WERE AT A LOW LEVEL.

7. WE WISH WE COULD FORECAST A FASTER GROWTH RATE FOR NEXT YEAR BUT CANNOT. THE WHEAT CROP, TO BE HARVESTED IN SPRING, WILL AGAIN BE DISAPPOINTING, AND OFFICIALS FEAR IT MAY BE THE SMALLEST IN THREE YEARS. MOREOVER, BOTH THE IMF AND PAKISTAN STATE BANK GOVERNOR HAVE RECENTLY WARNED THAT THE RATE OF DOMESTIC SAVING AND INDUSTRIAL INVESTMENT HAVE BEEN DECLINING IN RECENT YEARS AND THIS TREND MUST BE REVERSED. WHILE SOME INCREASE IN PUBLIC INVESTMENT IS GOING ON (SUGAR MILLS, FERTILIZER PLANTS, REFINERIES, STEEL MILLS), LIMITED OFFICIAL USE

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AND SOME HOPEFUL SIGNS OF A MODEST RISE IN PRIVATE INDUSTRIAL INVESTMENT EXIST, THE LAGS AND MAGNITUDES INVOLVED WILL NOT HELP 1975 VERY MUCH.

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8. LAST SUMMER THE GOP ESTIMATED THAT REAL GNP GROWTH IN
FY 74 (NO CY GNP FIGURES ARE KEPT) WAS 6.1 PERCENT AND PER
CAPITA GNP GROWTH 3.1 PERCENT. THESE FIGURES WERE APPARENTLY
UNREALISTICALLY HIGH. IN NOVEMBER A VISITING IBRD TEAM
MEMBER ESTIMATED THAT BECUASE OF THE SMALLER THAN ESTIMATED
WHEAT CROP LAST SPRING AND OTHER FACTORS, OVERALL REAL
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GROWTH MAY HAVE BEEN AS LOW AS THREE PERCENT. THIS WOULD
PUT THE PER CAPITA GNP GROWTH RATE AT ABOUT ZERO.

9. IF THESE LAST ESTIMATES ARE REASONABLY ACCURATE, THEY
MUST COME AS A DISAPPOINTMENT TO CONCERNED GOP OFFICIALS.
SINCE PAKISTAN'S ANNUAL GROWTH RATE HAD ONLY AVERAGED 3.6

PERCENT AND PER CAPITA GNP 0.6 PERCENT OVER THE PREVIOUS FIVE YEARS, PAKISTAN IS BY NO MEANS DEVELOPING QUICKLY OR RAPIDLY ENOUGH.

10. AN IMPORTANT RELATED QUESTION IS WHETHER POPULATION GROWTH IS OUTSTRIPPING FOOD PRODUCTION. THE CURRENT INDICATORS ARE NOT ALL THAT CLEAR BUT WE THINK NOT IN TERMS OF PAST TRENDS. UNFORTUNATELY, IT DID HAPPEN LAST YEAR WITH WHEAT (THE MOST IMPORTANT FOOD HERE) AND WILL HAPPEN AGAIN WITH THIS ITEM THIS YEAR. AS COMPARED TO A POPULATION GROWTH RATE OF 3 PERCENT PER ANNUM, WHEAT OUTPUT IN FY 74 ROSE BY ONLY 2.5 PERCENT AND MAY DECLINE IN FY 75 BY 8 PERCENT OR MORE. HENCE THE FRANTIC CURRENT SEARCH FOR WHEAT IMPORTS OF 1.5 MILLION TONS. THE OUTLOOK FOR THE OTHER THREE MAJOR FOOD PRODUCTS (RICE, SUGAR AND VEGETABLE OILS) IS BETTER. RICE IS NOW THE SINGLE MOST IMPORTANT EXPORT ITEM, WHILE SUGAR OUTPUT IS ADEQUATE FOR DOMESTIC DEMAND. THE VEGETABLE OIL SITUATION IS HOWEVER PECULIAR. ALTHOUGH PRODUCTION HAS BEEN EXCEEDING POPULATION GROWTH, INTERNAL DEMAND HAS BEEN CLIMBING EVEN FASTER. THUS THE GOP DECISION TO IMPORT 145,000 TONS THIS FISCAL YEAR.

11. UNEMPLOYMENT. WE CAN ALSO NOT POINT TO ANY IMPROVEMENT IN THIS CATEGORY. IN CY 1974, THERE WAS CERTAINLY AN INCREASE IN THE TOTAL NUMBER OF THOSE UNDER-EMPLOYED AND UNEMPLOYED, AND IN PERCENTAGE TERMS THE SHARE OF THE WORK FORCE IN THESE CATEGORIES PROBABLY INCREASED SLIGHTLY TO ABOUT 25 PERCENT. PROSPECTS FOR SOME IMPROVEMENT IN 1975 ARE UNFORTUNATELY NOT GOOD. NO PROBLEM IN PAKISTAN IS MORE DIFFICULT TO SOLVE.

12. THE DIMENSIONS OF THE PROBLEM CAN BE GAUGED FROM A FEW SIMPLE BUT DEPRESSING FACTS. SINCE OPPORTUNITIES FOR ADDITIONAL EMPLOYMENT IN RURAL AREAS ARE SMALL, INDUSTRY OFFERS THE BEST POTENTIAL FOR ABSORBING THE SURPLUS WORK FORCE. LIMITED OFFICIAL USE

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YET, THE CURRENT ANNUAL INCREMENT (OF ABOUT 600,000 WORKERS) TO THE COUNTRY'S LABOR FORCE IS NOW MORE THAN THE TOTAL NUMBER OF PERSONS EMPLOYED IN ALL FACTORIES WITH TEN WORKERS OR MORE. WITH THE URBAN POPULATION GROWING AT ALMOST TWICE THE OVERALL POPULATION RATE, UNDER-EMPLOYMENT AND UNEMPLOYMENT APPEAR TO BE INCREASING. AN IBRD STUDY LAST YEAR GLUMLY CONCLUDED THAT UNDER PRESENT CIRCUMSTANCES "THERE IS NO EVIDENT WAY OF AVOIDING INCREASING UNDER-EMPLOYMENT AND GREATER INEQUALITIES IN INCOME."

13. THIS IS GENERALLY DEPRESSING PICTURE BUT THE LONGER-RUN PICTURE GIVES SOME GROUNDS FOR HOPE. ONE IS THAT PAKISTAN'S GROWTH IN THE PAST HAS BEEN CHARACTERIZED BY SIZEABLE

GNP SWINGS. WE MAY BE JUST IN A DOWN PERIOD. WITH MASSIVE OIL-COUNTRY AID SUPPLEMENTING TRADITIONAL AID DONORS, PRODUCTION WILL RISE AND UNEMPLOYMENT COULD DECLINE. FURTHERMORE, SINCE INDEPENDENCE 28 YEARS AGO, PER CAPITA LIVING STANDARDS IN PAKISTAN HAVE BEEN CLIMBING PERCEPTIBLY THOUGH SLOWLY. THERE IS NO STARVATION IN PAKISTAN AND ADJECT POVERTY SEEMS LESS VISIBLE THAN TWO DECADES AGO. ANOTHER HEARTENING FACT IS THAT THE BHUTTO GOVERNMENT IS NOW VERY MUCH CONERNED OVER THE COUNTRY'S 3 PERCENT POPULATION GROWTH RATE. WITH U.S. AND OTHER FOREIGN HELP, IT IS BEGINNING TO TACKLE THIS MAJOR SOURCE OF THE UNEMPLOYMENT PROBLEM. THE PRESENT EFFORT MAY BE LESS THAN WHAT MANY EXPERTS CLAIM IS IMPERATIVELY NEEDED (THE UN TARGET RATE IS 1.7 PERCENT POPULATION GROWTH RATE), BUT THE WILL AND COMMITMENT ARE THERE.

14. INFLATION. THE RATE OF INFLATION IN CY 1974 APPEARS TO BE SLOWING AS COMPARED TO THE VERY BAD YEAR OF 1973. WHEREAS IN THAT EARLIER YEAR PAKISTAN EXPERIENCED AN INFLATION RATE OF 32 PERCENT (WHOLESALE PRICE INDEX), THE RATE FOR CY 74 DROPPED TO ABOUT 21 PERCENT (BASED ON A FIRST ELEVEN MONTHS PROJECTION). FOR 1975, THE RATE IS LIKELY TO REMAIN HIGH: BETWEEN 20-25 PERCENT. WE AGREE WITH THE IMF THAT THE MAIN PRESSURES BEHIND PAKISTAN'S INFLATION HAVE BEEN EXTERNAL: MUCH HIGHER PRICES OF IMPORTED PETROLEUM, AGRICULTURAL PRODUCTS, AND MACHINERY. UNLESS THESE EXTERNAL PRICES MODERATE, PAKISTAN WILL FIND IT DIFFICULT TO REDUCE INS INFLATION BELOW DOUBLE FIGURES.

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15. THE GOP IS NONETHELESS RESPONSIBLE FOR SOME OF THE INFLATION. DEFICIT FINANCING AND A VERY INCOME INELASTIC TAX STRUCTURE HAVE CONTRIBUTED TO PRICE PRESSURES. DEFICIT FINANCING IN 1975 MAY BE EVEN LARGER THAN LAST YEAR. IT MAY REACH RUPEES 1.6 BILLION IN FY 75, OR 4-5 PERCENT OF THE MONEY SUPPLY AS OF THE END OF JUNE 1974.
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16. THE MOST INTERESTING ASPECT OF THE INFLATION PICTURE HAS BEEN THE ABILITY OF THE PUBLIC TO ADJUST TO IT, DESPITE MUCH GRUMPLING. THIS APPEARS DUE TO THE FACT THAT THREE-QUARTERS OF THE POPULATION IS RURAL AND LARGELY SELF-SUFFICIENT, AND THAT OF THE QUARTER OF THE POPULATION LIVING IN URBAN AREAS PERHAPS 80 PERCENT IS MADE UP OF SMALL SHOP-KEEPERS, SERVICE ENTREPRENEURS AND SMALL MANUFACTURERS. ALL THESE GROUPS FIND IT EASY TO RAISE THE PRICES OF THEIR PRODUCTS OR SERVICES TO COPE WITH THE GENERAL INFLATION. THE ORGANIZED URBAN INDUSTRIAL WORKERS HAVE ALSO BENEFITED FROM GOP WAGE POLICIES. THE CATEGORY MOST ADVERSELY AFFECTED HAS BEEN THAT OF GOVERNMENTEMPLOYEES WHOSE SALAREIS HAVE TENDED TO LAG BEHIND THE INFLATION.

17. PAKISTAN HAS PROFITED IN ONE MAJOR WAY FROM THE INTERNATIONAL INFLATION. THE REAL GRANT ELEMENT IN ITS LARGE FOREIGN DEBT HAS UNDOUBTEDLY INCREASED WITH THE DEPRECIATION IN VALUE OF THE MAJOR INTERNATIONAL CURRENCIES. MOREOVER, THE INTEREST RATES IT OBTAINED ON PAST LOANS NOW LOOK PRETTY GOOD AGAINST PRESENT-DAY TERMS.

18. IN SUM, WHILE PAKISTAN HAS MANAGED TO ROLL WITH THE BLOWS OF INFLATION AND WILL PROBABLY DO SO AGAIN THIS YEAR.

19. BALANCE OF PAYMENTS. AFTER REGISTERING SURPLUSES FOR TWO STRAIGHT YEARS, PAKISTAN EXPERIENCED A SHARP BALANCE-OF-PAYMENTS DEFICIT IN CY 1974. PRELIMINARY FIGURES INDICATE IT WAS ABOUT \$225 MILLION. (THE TRADE DEFICIT WAS ABOUT \$640 MILLION AGAINST A DEFICIT OF \$103 MILLION IN 1973.) FY CY 1975, THE OUTLOOK IS FOR AN EVEN BIGGER DEFICIT; PERHAPS \$380 MILLION. (THE GOP ITSELF PREFERS TO MEASURE THE BALANCE OF PAYMENTS ON A FISCAL YEAR BASIS. BY THAT MEASURE, IT REGISTERED A DEFICIT IN FY 74 ON \$148 MILLION.)

20. FOR FY 1975 (AS AGAINST CY 75) GOP ECONOMISTS ESTIMATE THE DEFICIT TO BE BETWEEN \$290-350 MILLION, WHICH IS NOT MUCH DIFFERENT FROM THE IMF ESTIMATE OF TWO MONTHS AGO OF \$300 MILLION. HOW THIS DEFICIT WILL BE FINANCED IS AT PRESENT UNCLEAR. PAKISTAN'S RESERVES ARE OFCOURSE LARGE ENOUGH TO COVER ANY OF THE ABOVE ESTIMATED SHORTFALLS. LIMITED OFFICIAL USE

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FURTHERMORE, PAKISTAN EXPECTS TO DRAW ON ITS NEW IMF STANDBY ARRANGEMENT.

21. WHILE THERE IS THEREFORE MUCH TO BE PESSIMISTIC ABOUT IN THE B/P OUTLOOK, THERE ARE TWO ENCOURAGING DEVELOPMENTS IN THE PICTURE. ONE RELATES TO PAKISTAN'S ABILITY TO SERVICE ITS FOREIGN DEBT. THE IMF HAS CALCULATED THAT AS LONG AS THE COUNTRY'S EXPORT EARNINGS GROWN BY AT LEAST 14 PERCENT ANNUALLY FOR THE NEXT SIX YEARS, IT WILL BE ABLE TO MAINTAIN ITS DEBT-TO-EXPORT EARNINGS RATIO AT OR BELOW 20 PERCENT. IN CY 1974, PAKISTAN PROBABLY ACHIEVED AN 18 PERCENT GROWTH RATE IN EXPORT EARNINGS, AND THERE IS EVERY REASON TO BELIEVE IT WILL COME CLOSE TO THE 14 PERCENT LEVEL IN CY 1975, AND EVEN DO SOMEWHAT BETTER ON A FISCAL YEAR BASIS.

22. THE OTHER RELATES TO THE HUGE AID INPUTS AND COMMITMENTS COMING FROM THE OIL-RICH MIDDLE LEASTERN COUNTRIES. IN CY 74 PAKISTAN RECEIVED COMMITMENTS ORCASH FROM THESE SOURCES OF OVER \$800 MILLION (OF WHICH DISBURSEMENTS CAME TO \$290 MILLION). AND IN THE FIRST TWO WEEKS OF 1975, AID DONATIONS FROM THESE COUNTRIES FOR THE SWAT EARTHQUAKE DISASTER REACHED A SPECTACULAR \$40 MILLION, FAR IN EXCESS OF PAKISTAN'S NEEDS FOR THAT CALAMITY. GOP OFFICIALS ARE OPTIMISTIC THAT THEY CAN CONTINUE TO RECEIVE SUBSTANTIAL ASSISTANCE FROM THEIR OIL PRODUCING MOSLEM NEIGHBORS, PROVIDED THE COUNTRY IS ABLE TO DEMONSTRATE IT CAN USEFULLY APPLY THIS ASSISTANCE. LUPPI

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Message Attributes

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